

Next chapter of U.S.-Canada trade war: What we know and don't about Section 338 tariffs

RBC Economics · viktoriyapanahova · 2026-08-22 · English original

With no last-minute deal to avoid new section 338 tariffs, new tariffs have now officially taken effect on another subset of U.S. imports from Canada.

As we noted previously, the measures apply a 50% tariff rate on U.S. imports accounting for about 5% of Canadian exports to the United States – adding to existing tariffs on products like steel and aluminum, lumber, and motor vehicles.

As we argued a month ago when the tariffs were initially announced, the size of the tariffs is likely not large enough to derail Canada's economic growth backdrop. The Canadian value added content of newly tariffed U.S. imports adds up to ~0.4% of Canadian GDP and jobs. More than 80% of exports would remain duty free under CUSMA exemptions.

Still, the measures mark a re-intensification of U.S. tariff threats/measures, and concentrated specifically on Canada. Here we outline what we know, and what we don't know, about new measures and key questions that will need to be answered in the days ahead.

What we know:

For specific sectors targeted, the impact will be significant

These tariffs are different than previous measures in that, at least on paper, it appears that U.S. importers would have a significantly easier time than Canadian exporters diversifying to alternative markets.

By our earlier count, about 3.7% of total U.S. imports of products targeted come from Canada in 2025 while the U.S. accounted for 81% of Canadian exports of those products.

Plastic products, electrical machinery, furniture and wood product sectors are among the most significantly impacted by the new measures – and regionally that means a higher concentration of economic impact in Quebec, BC, and Ontario.

Because the tariff rate is so high and applies only to Canada, purchases of these products from Canada would be prohibitively expensive.

Canada's average effective tariff rate mechanically would rise to around 6% from around 3%—no longer the lowest among major U.S. trade partners, but still below the average U.S. tariff rate on imports from all countries (close to 7%). In practice, the observed tariff rate will not increase that much, because many of these highly tariffed products will simply not be traded. But the economic cost of the increase is real nonetheless.

What we don't know yet:

Prior tariffs imposed by the U.S. administration have been modified or dropped in the weeks following the initial imposition of measures.

That includes briefly imposed blanket tariffs on imports from Canada imposed in March 2025 before the CUSMA exemption that has since protected the bulk of Canadian exports from tariffs was imposed days later.

And an exemption list from broader U.S. tariffs imposed on all trade partners (the current section 301 tariff regime that replaced the section 122 measures that temporarily replaced the IEEPA tariffs struck down by the U.S. supreme court in February) has grown to cover more than half U.S. imports.

But the U.S. and Canadian sides have reportedly cut off negotiations, leaving the path to end the current additional tariffs highly uncertain.

At time of writing Canada has not yet announced a specific response to the new U.S. tariffs but has signaled plans to impose retaliatory measures.

In general, retaliatory measures typically add costs to domestic (Canadian) imports rather than hurting foreign country exporters.

But a nuance in this case is that Canada is actually a net importer of products on the new section 338 tariff list from the United States – Canada imported about \$23 billion USD of the products targeted from the U.S. in 2025 compared to about \$20 billion USD of exports.

On paper, that means that redirecting imports of these specific products to instead purchase from Canadian sellers that otherwise would have been shipping to the United States mechanically could actually fully replace lost U.S. exports.

The reality is that would not be so simple – supply chains are heavily integrated so there are exporters/importers on both sides of the border that will see a significant increase in costs as a result of new tariffs.

But there is likely more potential for trade flows to reorient within North America to avoid increased tariff costs with these measures than some of the other sector specific tariffs imposed to-date.

Will business sentiment/investment falter?

Most (more than 80%) of Canadian exports to the U.S. would remain tariff free under new tariffs – but the unpredictability of U.S. administration tariff policy means it is not possible for businesses to predict which sectors might be next. And that unpredictability is a weight on business confidence across all trade exposed industries, not just those directly targeted with tariffs.

Still, businesses have been showing signs of adapting to living under uncertainty after a year and a half of tariff threats with measures of business confidence and investment perking up to-date in 2026.

We do not expect the broader macroeconomic impact of these new tariffs to be enough to push the Bank of Canada to seriously consider pivoting to interest rate cuts.

Tariff economic growth headwinds are still relatively narrowly based in a smaller number of highly impacted industries and fiscal (government tax and spending) policy is still better suited to provide targeted relief than blanket changes in interest rates from the central bank – and there are reports that fiscal supports will follow the imposition of this latest tariff round.

Still, the intensification of trade uncertainty and recent moderation in underlying (excluding energy products) inflation trends also has increased the likelihood that the BoC will not hike interest rates this year.

What does it mean for broader CUSMA negotiations?

The section 338 tariff measures imposed further erode the share of Canadian exports protected by CUSMA, but more than 80% of Canadian exports should continue to cross the border duty free under current rules.

CUSMA itself does not expire for a decade, and the agreement requires negotiations in the mean-time to try and extend the deal before then. But the threat of additional tariffs will remain.

Still, the broader CUSMA exemption has held through multiple forms of broader U.S. tariff policies, including the current section 301 global tariff measures. U.S. average tariff rates globally have been drifting lower rather than higher with the list of broader products exempt from those section 301 tariffs rising to cover the bulk of overall U.S. imports.

While the future of U.S. trade policy is highly uncertain, we continue to argue that trade across the Canada and U.S. border is mutually beneficial, and that argues for the bulk of trade to remain tariff free under CUSMA.

This article is intended as general information only and is not to be relied upon as constituting legal, financial or other professional advice. The reader is solely liable for any use of the information contained in this document and Royal Bank of Canada ("RBC") nor any of its affiliates nor any of their respective directors, officers, employees or agents shall be held responsible for any direct or indirect damages arising from the use of this document by the reader. A professional advisor should be consulted regarding your specific situation. Information presented is believed to be factual and up-to-date but we do not guarantee its accuracy and it should not be regarded as a complete analysis of the subjects discussed. All expressions of opinion reflect the judgment of the authors as of the date of publication and are subject to change. No endorsement of any third parties or their advice, opinions, information, products or services is expressly given or implied by Royal Bank of Canada or any of its affiliates.

This document may contain forward-looking statements within the meaning of certain securities laws, which are subject to RBC's caution regarding forward-looking statements. ESG (including climate) metrics, data and other information contained on this website are or may be based on assumptions, estimates and judgements. For cautionary statements relating to the information on this website, refer to the "Caution regarding forward-looking statements" and the "Important notice regarding this document" sections in our latest climate report or sustainability report, available at: <https://www.rbc.com/community-social-impact/reporting-performance/index.html>. Except as required by law, none of RBC nor any of its affiliates undertake to update any information in this document.

Source: <https://www.rbc.com/en/economics/canadian-analysis/featured-analysis/insights/next-chapter-of-u-s-canada-trade-war-what-we-know-and-dont-about-section-338-tariffs/>